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E.O. 12958: N/A
TAGS: EPET ENRG EMIN EINV EIND ETRD ELAB KHIV SF
SUBJECT: South Africa: Minerals and Energy Newsletter "THE ASSAY" - Issue 4, 1-15 March, 2008

This cable is not for Internet distribution.

¶1. (SBU) Introduction: The purpose of this newsletter, initiated in January 2004, is to highlight minerals and energy developments in South Africa. This includes trade and investment as well as supply. South Africa hosts world-class deposits of gold, diamonds, platinum group metals, chromium, zinc, titanium, vanadium, iron, manganese, antimony, vermiculite, zircon, alumino-silicates, fluorspar and phosphate rock, and is a major exporter of steam coal. South Africa is also a leading producer and exporter of ferroalloys of chromium, vanadium, and manganese. The information contained in the newsletters is based on public sources and does not reflect the views of the United States Government. End introduction.

HOT NEWS

DRC Mineral Contract Review

¶1. (SBU) Mining is again booming in the DRC, although the government's mining contract review has created some uncertainty. The DRC's once mighty mining sector, with a treasure trove of largely unexploited concessions, saw its output of copper, cobalt and diamonds decrease and its infrastructure crumble during years of conflict, corruption and neglect. The old Congo produced around 500,000 tons of copper per year in the 1980s, but just 17,000 tons in 2005. Since the confirmation of Joseph Kabila as President, some stability has returned to the DRC and mining is again booming. The huge province of Katanga has seen large investments from international mining companies such as Freeport McMoran, De Beers, BHP Billiton, and from a large number of medium and junior exploration and mining companies such as First Quantum (Australian) and Metorex Mining (South African). Many mineral contracts were issued during the years of turmoil, which the Kabila government considers to be one-sided in the favor of companies. The government therefore set up a Review Panel in 2007 to re-evaluate (and renegotiate) all mineral contracts to ensure that the DRC receives a larger slice of the benefits from its mineral resources.

¶2. (SBU) The DRC government released its Mining Contract Review

Report in mid-March. The review panel recommended steps to overhaul the country's minerals sector including renegotiating several major mining contracts and cancelling others. The report stated that the government intended to ensure efficient management and adequate control of the mining sector so that Congolese mines benefited the Congolese nation. The report recommends:
-- renegotiation of the contract between state mining company Gecamines and Freeport-McMoran for the development of the Tenke Fungurume project
-- renegotiation of contracts between state diamond miner MIBA and BHP-Billiton and De Beers
-- increasing state mining company OKIMO's stake in the Kilo Gold joint venture with AngloGold Ashanti from 13.8 percent to 45 percent

-- increasing the annual fee paid to OKIMO by AngloGold
-- cancelling contracts awarded to some smaller companies.
Q companies.
No mention was made as to how or who would pay for the increased stakes for state and local companies.

GOLD

Re-Opening Central Rand Gold Mines

¶3. (SBU) Central Rand Gold (CRG) was formed to mine gold ore and reefs left behind in SA's central rand gold district where mining ceased in the 1970's. CEO Greg James recently announced an increase

of 1.76 million ounces in the company's gold resources, bringing the total resource to 35.5 million ounces. The company has identified three probable targets for shallow mining of the Kimberley Reef group and the Main Reef group at their property west of Johannesburg. CRG plans to begin production at a rate of 100,000 ounces per annum by the end of 2009, 250,000 ounces in 2010, and 1 million ounces by 2012. CRG expects to receive its mining license in August, clearing the way to begin mining over a 40-kilometer deposit strike length.

¶4. (SBU) The land CRG has applied for was mined by a number of companies for decades leading up to the 1970s. Those companies targeted the high-grade Main Reef, whereas CRG plans to mine the lower grade Kimberley and Bird Reefs, which have become economic at the increased gold price. Waste dumps that previously covered shallower parts of the reefs have largely been retreated, opening the way for renewed mining operations. CRG has also been approached by groups interested in potential uranium byproducts, but James said talks have been put on hold so that the company can focus on bringing the project to fruition and on completing legislated social and labor plans and the environmental impact assessment (EIA). Five existing shafts have been re-opened to allow for sampling between the 130 and 300-meter levels below the surface.

POWER CRUNCH

BHP-Billiton to Cut Aluminum Production

¶5. (SBU) Aluminum smelting is the most energy intensive of all mineral processing operations. About 1MW of electricity is needed to produce 500 tons of aluminum metal. BHP-Billiton's three plants, two in KwaZulu/Natal Province and one near Maputo in Mozambique, produce some 1.2 million tons of aluminum metal per year and require a total of about 2,400MW of power. This is equivalent to the power needed for the rest of the KwaZulu/Natal Province. Eskom is

searching to save every megawatt it can and the "buy-back" of power from aluminum smelters is high on its list of priorities. Aluminum smelters also require a virtually uninterrupted supply of power and any cut lasting more than four hours has the potential to cause the metal to freeze in the smelter pots, which would cause massive and costly damage to the plant. (Comment. BHP Billiton's spokesperson confirmed to media publication Mining Weekly Online that the company has taken a corporate decision to phase out its business links with Standard Bank, after the Standard Bank's Chairman suggested at a Business Leadership meeting with government that BHP-B shut down its power-heavy Richards Bay Hillside aluminum smelter because it added little value to the economy. End Comment.).

¶6. (SBU) Eskom's announced 10 percent power cut to BHP-B's aluminum smelters is insufficient to sustain full production. The company has thus decided to close 120,000 tons of output, which will allow the remaining facilities to operate at full power. This will allow Qthe remaining facilities to operate at full power. This will allow Eskom to recover 240MW of power, but is likely to cause BHP-B and SA to lose nearly $340 million in annual revenues and foreign exchange respectively, place an estimated 800 jobs in jeopardy, damage SA's reputation as an investment destination, and postpone Rio Tinto-Alcan's decision to go ahead with a new $2.7 billion 720,000-ton aluminum smelter at Coega, at least until Eskom can guarantee an adequate and reliable power supply. Rio Tinto, the SAG, and Eskom are currently reviewing the terms of the Coega smelter project in order to align its timing with the availability of future generation capacity. Rio Tinto-Alcan has said that it would work with the SAG to minimize the impact of the potential rescheduling on regional economic development.

ENVIRONMENT

Fertilizer Company Gets Credit for Carbons

¶7. (SBU) Diversified chemical and fertilizer company Omnia announced on March 17 its 15-million Euro agreement with the International Finance Corporation (IFC) for the purchase of up to one million carbon credits from Omnia over the next five years. The Omnia Clean Development Mechanism (CDM) project Envinox could generate 420,000 Certified Emission Reduction (CER) credits per year from the nitrous oxide destruction facility installed at their nitric acid plant at Sasolburg (nitrous oxide is a green-house gas). Omnia has indicated that carbon credits generated by the plant could add about $7.5 million per year to the company's revenues. This is the first carbon delivery guarantee agreement of its kind in sub-Saharan Africa, and only the second in the world, whereby the IFC mitigates the country and project risk, making the carbon credits accessible to a wider range of international buyers. According to the IFC Southern Africa Region Manager, the IFC has committed to purchase a minimum of 50 percent of Omnia's CERs for the next five years and guarantees delivery of the credits to buyers under the Kyoto Protocol.

Green Light for New Power Station

¶8. (SBU) South Africa's Environmental Affairs and Tourism Minister dismissed appeals against construction of Eskom's new 5,400MW coal-fired power station Project Bravo, planned for Witbank in Mpumalanga Province. The plant is part of Eskom's plans to boost generation capacity to alleviate the country's current serious capacity shortfall. The plant is to be fitted with the most advanced air pollution abatement equipment installed in a South African power station, including flue-gas desulphurization technology to remove 90 percent of the sulfur dioxide (SO_2) from the emissions. The Minister also said Bravo should be carbon-capture-ready and would have to submit a report detailing preferred capture technology options before proceeding with

construction.

MINING LEGISLATION

SAG to Review Latest Draft of Royalty Bill

¶9. (SBU) The first draft of SA's Royalty Bill was issued in 2003, following the 2002 approval of the Mineral and Petroleum Resources Development Bill (MPRDA), which legislated that all mineral rights must revert to the custodianship of the SAG. The Royalty Bill will govern the way mining companies are taxed on their production. Initial reaction from industry to the first draft was negative because rates were based on gross mineral revenues and were also considered to be too high. Since then, the Department of Finance (which is ultimately responsible for the bill), Industry and the Department of Minerals and Energy (DME) have been in negotiation and a number of revised drafts have been issued for comment. The third and supposedly final draft was released for public comment in December 2007. This draft uses a formula to calculate royalty rates payable for each mine. The mining industry has accepted this
Qpayable for each mine. The mining industry has accepted this
formula in principle, but calculations have shown some unintended consequences. Namely, the bill has not taken into consideration the huge increases in commodity prices nor the escalating capital costs of new mines and mine expansions, and this has resulted in calculated rates being higher than those proposed in the 2003 draft.

¶10. (SBU) The mining industry and labor have raised concerns over the effect the latest draft would have on production and employment in the country's mining sector, which is already struggling with reduced and uncertain power supply, rising production costs and a shortage of skilled workers. Minerals and Energy Minister Buyelwa Sonjica said that the SAG had taken note of mining industry concerns and her department would hold talks with the Department of Finance on the issue. She also said she did not expect the bill to be promulgated in its current form. She said there was a fine line

between ensuring that locals derive economic benefit from mining without deterring valuable foreign investment.

ENERGY

Eskom's Massive Price Hike Sparks Reaction

¶11. (SBU) Power utility Eskom's call for a 53 percent electricity tariff increase (on top of the 14.2 percent increase already granted) has met with concern by analysts, economists, trade Unions, and the ruling ANC Party, all expressing anxiety over the impact on inflation and on the economy, industry and South African consumers. A leading economist said that the increase would take $4.5 billion out of the economy, and equates to a 1.8 percent increase in the interest rate, already at 14.5 percent for borrowers.

Westinghouse Included as PBMR Partner

¶12. (SBU) South Africa's advanced nuclear reactor program PBMR (Pebble Bed Modular Reactor) has announced that it has finalized a new shareholders agreement with U.S. company Westinghouse Electric making it a partner in the project. Westinghouse already held a 15 percent share in PBMR, but legislation required the implementation of a new shareholder agreement, which offered Westinghouse an important opportunity to highlight its commitment to South African nuclear technology as it competes head-to-head with Areva of France for up to 20,000 megawatts of new nuclear power build through 2025. The SAG aims to include PBMR as part of its new nuclear build mix.

Other partners in PBMR include state-owned Eskom and the Industrial Development Corporation. The high-temperature, helium-cooled PBMR technology aims to improve safety and efficiency by employing 165MW modules and nuclear fuel sealed in tennis ball-sized graphite "pebbles".

Sasol Looks at CTL to Cut Oil Imports

¶13. (SBU) The Sasol board announced its commitment to the proposed new 80,000 barrel-per-day coal-to-liquids plant project dubbed "Mafutha", by deciding to spend $40 million on feasibility studies for the project, whose location is yet to be determined. Sasol CEO Pat Davies stated that the plant would be built so as to be carbon-capture-ready, with the disposal of the CO2 to be determined as part of the feasibility study. Davies also said that Sasol was working with Eskom and the government "to see what else we can bring to bear using our technology and our feed-stocks to alleviate South Africa's electricity shortage", but stressed that Sasol's primary function was to keep the country "wet as far as fuels are concerned". Sasol earlier announced a joint venture with Mozambique to construct a $157-million gas compression station at the border to facilitate a 20 percent expansion of natural gas delivery. Sasol clarified that the additional gas from Mozambique would be for its own needs to reduce reliance on the Eskom grid, and not available for other companies' cogeneration projects. Sasol separately
Qfor other companies' cogeneration projects. Sasol separately
announced a 15 percent increase in operating profits for second half 2007 due to high oil prices, but offset somewhat by the stronger rand in 2007 and losses on an oil hedge. Sasol also unveiled final terms for its $3 billion BEE transaction aimed at addressing skills development in science and technology.

Sasol Confident on China Business Risks

¶14. (SBU) Sasol is the world's leading producer of liquid fuel from coal (CTL) and is busy with the second phase of a bankable feasibility study for two CTL plants in China. General Manager for International Energy Leon Strauss said Sasol had secured favorable participation for itself in the project. Studies undertaken between

2002 and 2005 in Shaanxi Province and the Ningxia Hui region indicated that two CTL liquid fuels plants, together with dedicated coal mines, were feasible. Each plant would have a production capacity of 84,000 barrels per day. If the go-ahead is given, the plants will likely come on stream around 2017. However, Sasol CEO Pat Davies pointed out that there is a massive demand for skilled people in the energy sector, making the completion of projects on time and on budget very difficult.

¶15. (SBU) Because of Sasol's concerns about the protection of intellectual property rights (IP) in China, the first phase of the bankable study put in place economic enablers, including securing Sasol's participation in the CTL project. Strauss declined to say what the ownership structure would be, but stressed that Sasol would not embark on multi-billion dollar projects in China without a sizeable stake of around 50 percent in the projects. He said Sasol only looked at commercial opportunities that gave appropriate reward for the risk of taking their IP to China, but he said Sasol was confident with both projects. Strauss said the way was clear for Sasol to go into a full-blown feasibility study and the Sasol Board had approved this phase in December 2007. A tender went out in January for international contractors to assist in the process and the preferred bidder is to be decided in May. The end of 2009 should see completion of the feasibility study for the two Chinese projects.

New Biodiesel Plant for Coega

¶16. (SBU) Coega is SA's new deep-water port and economic development zone (EDZ), which is under construction on the south coast of the Eastern Cape Province. The SAG decided to build the port to boost economic development in one of the country's poorest provinces, and the EDZ authority has sought to encourage key industries to establish operations in the zone. A new client is Australian-owned firm Rainbow Nation Renewable Fuels (RNRF), which has applied for a license to produce 288 million liters of biodiesel a year from a $2-billion plant being built at Coega. The plant will be the biggest in Africa, using one million tons of soybeans to produce 250,000 tons of soybean oil and 800,000 tons of animal feed. A portion of the oil will be used to produce biodiesel. RNRF MD Geoff Mordt said that the plant would be commissioned in late 2009 and the company had secured a 48MW power supply.

¶17. (SBU) A major concern for all biofuel projects is the likely impact on local food supply and prices. Initially, the bulk of RNRF's soybean feedstock will be imported. South Africa's current production is about 300,000 tons per year and Mordt said that the plant would support local commercial and small-scale farmers to increase the country's production from currently unused land. In this way, South Africa could source nearly 100 percent of the required soybean feedstock within five years. RNRF must comply with BEE Charter requirements by selling a stake in the company to
QBEE Charter requirements by selling a stake in the company to black-owned companies. Mordt said that the operation would create 350 new direct permanent jobs and 725 indirect jobs.

AFRICA IN BRIEF

Electricity Expansion in Mozambique

¶18. (SBU) For years Mozambique has relied on its Cahora Bassa hydro-electric plant on the Zambezi River and the South African transmission network for its power supply. Its growing economy and the regional demand growth of 1,000MW per annum have necessitated planning for additional power. The Mozambican Finance Minister stated in mid-2007 that investments would be made to expand the country's electricity sector to connect more than one million people to the national grid. New power projects include:
-- 750MW gas-fired station in Inhambane Province
-- 2,000MW coal-fired station on the Moatize coalfield

in Tete Province
-- 1,200MW hydro-electric plant (Mpenda Nkua) in Tete Province at an estimated cost of $2.3 billion
-- $383 million expansion of the Cahora Bassa power plant from 2,000MW to 14,000MW.
Expansions to the power sector reflect the government's support for industrialization and its desire to attract foreign direct investment though the availability of cheap power, as it did to attract BHP-B's Mozal Aluminum Smelter. SA offers a ready market for this power.

Botswana's World-Class Diamond Centre

¶19. (SBU) The world's largest and most advanced diamond sorting facility has been opened in Gaborone. The Diamond Trading Company Botswana (DTCB), will sort and value all the rough diamonds produced by Debswana, and for the first time conduct local sales and marketing activities for rough diamonds - DTCB and Debswana are 50/50 partnerships jointly owned by De Beers and the Government of Botswana. De Beers said the initiative is expected to create a sustainable downstream industry, with approximately 3,000 new jobs in the cutting, polishing, sales, and marketing areas. DTC International will aggregate the majority of De Beers' global production in Botswana by 2009 instead of London.

Eskom Spurns Namibian Gas

¶20. (SBU) The medium-sized Kudu gas-field owned by NamPower and Tullow Oil (Irish) and operated by Tullow lies 170 kilometers off the Namibian coast. It was discovered by Chevron in 1973 and later jointly developed by Shell and Chevron-Texaco after numerous delays. Both companies decided to withdraw in 2003 and sold their Kudu stakes to Tullow Oil in 2004. The project has since been looking for a market for its gas. One option considered was to build a 400MW to 800MW gas turbine power station at Oranjemund, the diamond-mining town at the mouth of the Orange River, and sell 400MW of power to Eskom. Eskom has so far rejected any deal apparently because of price and foreign currency exposure. Until an agreement can be struck, Tullow intends to continue to investigate other options for the gas, including producing compressed and liquefied natural gas, and building a smaller power station to meet Namibia's needs.

Zambia Increases Mining Taxes

¶21. (SBU) Zambia's parliament approved an amendment to the Mines and Minerals Act on March 26 that will increase taxes and abolish existing agreements between the government and mining companies, according to the Zambian Chamber of Mines. The bill raises the effective tax rate on mining from 31 percent to 47 percent and will be signed into law by the President on April 1. The new dispensation will increase royalties on sales five-fold to 3 percent. Zambia is Africa's biggest copper producer and expects to earn an additional $450 million this year from the higher mining taxes.

BOST